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17 October 2017

John Pierce
Chairman
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PO Box A2449
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Submitted online: www.aemc.gov.au

Dear Mr Pierce

Submission on draft report: review of regulatory arrangements for embedded networks

Thank you for the opportunity to comment on the AEMC's draft report on its review of regulatory arrangements for embedded networks. We commend the AEMC on its thorough and insightful review of embedded networks (ENs) and identification of the key issues of EN regulation, including the lack of competition, the need for greater regulatory oversight of EN selling and improved customer protections for EN customers.

We generally support the AEMC's recommendations to remedy these matters. In doing so, we recognise the proposals are a significant shift in regulatory policy for EN operation and selling, and their adoption introduces a number of transitional and implementation challenges that will need to be considered and addressed. Our submission outlines these issues.

Opening embedded networks to competition

As indicated in our submission to the AEMC's consultation paper, we consider the introduction of competition in ENs constitutes the single most significant improvement to the operation of the EN market. In our view, improving EN customers' access to competition is likely to address many of the issues we currently see in this market.

Key measures to assist on-market transition

We agree that EN customers do not currently have adequate access to competition. As discussed in our consultation paper submission, providing EN customers with access to a retailer of choice will introduce competitive pressure into ENs, which should in turn improve customer service and competitive pricing as EN sellers compete to win and keep customers.

In its draft report, the AEMC has addressed this by proposing measures to simplify the processes for switching between the EN seller and other retailers, including requirements for:

- all new ENs to have an EN manager regardless of the number of customers in the EN
- EN managers to ensure every child meter is issued with a NMI regardless of whether customers are on- or off-market
- all ENs with an EN manager to appoint a metering coordinator to ensure on-market customers have market approved meters and have their metered usage recorded in MSATS
- all ENs with on-market customers to charge the market retailer (rather than the EN customer) the standing published local network service provider (LNSP) network tariff.

We consider these changes will eliminate key barriers to competition for EN customers. They will improve the ease of switching to a retailer by making EN customers discoverable in MSATS, standardising key market procedures and transactions, and overcoming the need for EN customers to receive supply from a retailer on energy-only contracts. In this way, market procedures for EN customers to switch retailers will be similar to those for grid-connected retail customers.

Additional measures to assist in on-market transition

To support these amendments we also suggest the following:

- record all EN customer meter data in MSATS (regardless of whether customers are on- or off-market) to simplify the process for EN customers moving from off-market to on-market contracts with other retailers
- require retailers to pass on payments for network services (NUoS) to EN operators. We understand some retailers at times withhold these payments, creating a barrier for EN customers to go on-market. This may also result in EN customers receiving two bills for network charges.

Summary of key points

- **Providing EN customers with access to a retailer of choice will improve customer service and pricing in ENs**
- **We consider the AEMC's proposed measures to simplify customer switching from off-to on-market will facilitate competition**
- **We propose additional measures to facilitate customer switching**

Elevating regulatory arrangements into energy laws

We support the AEMC's recommendation to require sellers to register with AEMO as an EN network service provider, and to hold a retailer authorisation from the AER (or seek exemptions for both from the AER).

AEMO registration

As noted in the draft report, the protections that exist due to the tripartite relationship between distributors, retailers and customers in the National Energy Retail Law (Retail Law) and National Energy Retail Rules (Retail Rules) are not fully extended to the majority of EN customers, though some do receive similar protections in particular aspects via the retail and

network exemptions frameworks. In the case of the EN operator-EN customer relationship, we consider requiring EN operators to register with AEMO as a market participant will improve EN operators' accountability to distributors, retailers and customers (for example, through appropriate reporting and compliance obligations). This, along with the significant amendments to the Retail Law and Rules referred to in the draft report, will afford equivalent or similar protections to EN customers as those afforded to customers via the distributor-customer relationship.

With its primary function the regulation of participant behaviour, we also suggest registration requirements be specifically targeted at EN operators and controllers rather than owners. Currently, these three functions are conjoined in the National Electricity Law (NEL) and given identical obligations in the Electricity Network Service Provider Registration Exemption Guideline (Network Guideline).¹ We suggest operation and control should be distinguished from ownership in the NEL, and compliance obligations placed specifically on operators and controllers as a requirement of AEMO registration, as we are primarily concerned about these parties' conduct given it is likely to have the most impact on EN customers.

We agree with the AEMC's position that a cost benefit analysis should not be required to establish new ENs, and consider the introduction of competition to ENs and greater regulatory oversight of new ENs will ensure that only networks offering actual customer benefits will be viable. While this is true of newly built ENs, we suggest that additional regulations may be required for approvals of embedded network conversions (retrofits). We note the proposed framework does not alter profit incentives for site owners/bodies corporate to retrofit existing sites, enabling them to collect LNSP network service charges from EN customers, and thus providing profit making opportunities. This profit incentive could involve a risk of EN creation in circumstances where there could be EN customer detriment. We consider the AEMC's proposed amendments to the framework balance this risk.

In assessing the impact of retrofit proposals on EN customers, the AER currently requires applicants to demonstrate a minimum of 85 per cent consent from EN occupants and to demonstrate a rigorous consent-gathering process. These requirements are attached to the current individual retail exemption application process and network registration process.² We suggest similarly rigorous requirements may need to be provided for in the proposed AEMO registration and/or retailer authorisation processes for ENs to ensure future retrofits have majority consent of EN occupants.

Benefits of EN authorisation and entry criteria

As with AEMO registration for EN operators, we consider the recommendation to require certain types of EN operators to be authorised will bring greater accountability and transparency to EN selling arrangements. In particular, requiring sellers to satisfy entry criteria and comply with most retailer obligations, will standardise energy selling arrangements in ENs and improve customer service obligations and protections.³

We suggest EN authorisation applicants be required to satisfy criteria currently applying to authorisations, covering proof of organisational and technical capacity, financial capacity and

¹ *AER Electricity Network Service Provider Registration Exemption Guideline (December 2016)*: <https://www.aer.gov.au/networks-pipelines/guidelines-schemes-models-reviews/network-service-provider-registration-exemption-guideline-december-2016> (see section 4.9).

² *AER Exempt Selling Guideline (March 2016)*: <https://www.aer.gov.au/retail-markets/retail-guidelines-reviews/retail-exempt-selling-guideline-march-2016> (see section 7).

³ This is likely result to in centralisation of energy selling to specialist retailers and away from site specific selling, as sellers who are unable to satisfy the requirements for retailer authorisation outsource energy selling to authorised EN sellers.

suitability. We note that the specific information requirements for EN authorisation applicants may not necessarily be the same as those that currently apply to authorisation applicants.

The need for flexibility in the Retail Law and Rules

While we support the AEMC's recommendation that EN selling arrangements be elevated to the Retail Law and Rules, and exemptions be reserved for a subset of on-selling arrangements, we see a number of risks with this proposal. Specifically, as discussed in our submission on the consultation paper, ENs have grown in popularity in recent years, as has the complexity and diversity of this sector of the market. By elevating regulatory arrangements into the Retail Law and Rules we risk losing some of the flexibility the AER currently has to regulate this disparate and evolving sector. This may have the unintended effect of stifling innovation or allowing new energy selling models to develop outside of the regulatory framework—both undesirable outcomes.

In elevating regulatory arrangements into the Retail Law and Rules, care therefore needs to be taken to ensure the benefits of greater regulatory certainty are achieved within a flexible framework that can encompass as yet unforeseen selling models. We support the AEMC's proposal to establish high level principles in the Retail Law for EN selling, and for the Retail Rules to provide additional guidance, provided there is sufficient flexibility to regulate new models as they evolve.

We also agree with the AEMC's intention to introduce flexibility to the authorisation framework by enabling the AER to impose additional obligations on authorised EN sellers where appropriate. It is important the Retail Law and Rules clarify our functions but provide sufficient flexibility so they are not overly prescriptive. This will ensure regulatory certainty for stakeholders while allowing the AER to regulate for changes in an evolving market. We welcome the opportunity to work with the AEMC in achieving this balance.

Retaining flexibility in the exemptions framework

A principles-based approach should equally be used in providing for a more limited exemptions framework. Examples of a principles-based approach include establishing eligibility based on whether energy is sold to a small number of customers or to large customers, where the cost of authorisation (or employing an authorised retailer) is likely to exceed the benefits to EN customers and a low level of regulatory oversight is required (for example the current deemed exemptions and all but the R1, R2, R3 and R4 registrable classes). A principles-based approach to identifying sellers eligible for exemptions is preferable to limiting eligibility to particular types of selling arrangements. It avoids precluding as yet unforeseen energy selling models from obtaining exemptions, where exemption may be more appropriate than authorisation.

We also consider caravan parks, whether for long-stay residents or holidaymakers, should be treated alike under the proposed framework. An unintended consequence of distinguishing between parks based on whether residents are long or short stay is that to meet the lower threshold (for example, exemption) new park operators may choose not to offer long term residency.

Improving compliance and enforcement responses

A particular benefit of authorisation and AEMO registration is greater transparency and accountability of EN operation and selling through reporting and increased oversight through monitoring. Given the diversity of EN operators and sellers, we consider it is important the AER has sufficient flexibility to determine an appropriate compliance and/or enforcement response. In our view, amendments to the National Electricity Rules (NER) and Retail Rules should provide guidance without imposing constraints through prescription.

We welcome the extension of compliance audit powers that will result from the proposed extension of the authorisation framework to a larger number of energy sellers. We also consider there is benefit in extending our current Retail Law and NEL powers to compel information and documents, to include the power to compel the examination of persons as is the case under section 155(1)(c) of the *Competition and Consumer Act 2010*. We are currently pursuing this amendment outside this review as we consider the power to require individuals to appear before the AER and give evidence will improve our ability to effectively investigate possible breaches of the Retail Law and Rules.

We also welcome the closer alignment of enforcement options for breaches of EN selling obligations. For consistency, we consider corresponding options should be available for breaches of network operation obligations, and network and retail exemption obligations. In particular, we propose that pecuniary penalties should reflect the provisions of the Australian Consumer Law and provide for different penalty amounts for different categories of participants:

- for individuals and corporations
- according to the type of organisation and its turnover.

Summary of key points

- **AEMO registration and retailer authorisation for EN sellers will result in greater transparency and accountability**
- **The AER's flexibility to regulate EN selling and operation should be preserved when elevating regulatory arrangements to the national framework**
- **Any additional options for compliance and enforcement should provide the AER with sufficient flexibility.**

EN customer protections

Core customer protections

We consider the same protections should apply to on-market and off-market customers, with the exception of retailer of last resort (RoLR) requirements. In particular, we support the proposal that under the new framework authorised EN sellers be required to provide core customer protections to EN customers as requirements of their authorisation and registration. They should include:

- information provision to prospective and current EN customers
- explicit informed consent from move-in customers to an EN
- notice of planned interruptions
- life support obligations
- obligations relating to the offer to supply
- establishing a designated retailer and standing offer for EN customers
- providing access to concessions in jurisdictions where customers cannot access these directly
- obligations relating to disconnection/de-energisation and reconnection/re-energisation (including minimum disconnection requirements currently applying to retailers)
- the requirement to be a member of a jurisdictional ombudsman scheme.

We note EN sellers' ability to deliver these protections relies in part on broader amendments to the retail market framework (for example, those discussed under "AEMO registration" above).

We agree with the AEMC's proposal to amend the authorisations framework to provide the AER with the flexibility to impose additional customer protections on retailers, where appropriate, to better meet the needs of customers in specific embedded networks.

While we do not consider it necessary for EN sellers to participate in the RoLR scheme, consideration should be given to managing EN retailer failure. The AER currently requires EN retailers to have back-up arrangements in the event of their failure, for example, for energy supply arrangements to revert to the relevant bodies corporate or landlords. Similarly, if the AEMC does not require RoLR scheme participation, other requirements to manage retailer failure should be considered.

Information provision

We support the AEMC's intention to align information provision requirements for EN operators with retailer obligations, and also agree that prospective EN customers should be given information to enable them to make better informed decisions about entry to an EN.

Price transparency

We agree with a need for greater price transparency for EN electricity and gas offers. We consider the best way to achieve this is by requiring EN sellers to publish their energy prices, fees and charges on their own websites in a form that is easy to compare with the tariffs, fees and charges of other sellers. As the AEMC suggests, this could be achieved by extending the obligations established in the AER's Retail Pricing Information Guidelines to cover EN published offers.

Summary of key points

- **The same protections should apply to off- and on-market customers**
- **While EN retailers do not need to participate in the RoLR scheme, consideration should be given to managing EN retailer failure**
- **To facilitate price transparency, EN retailers should publish offers on their websites.**

Additional matters

Managing dual frameworks and transitional issues

If the AEMC's recommendations are adopted major changes will need to be made to the market entry provisions of the Retail Law and Retail Rules and to the policies underpinning market entry. Potentially, the changes will result in the creation of a tiered authorisation framework that allows for full and conditional authorisations. Another consequence of the proposed changes will be some ENs being regulated under the exemptions framework and others under the authorisations framework. Legacy arrangements will continue in parallel with the new arrangements—potentially indefinitely—and regulation will be spread across two agencies, instead of one. In implementing the proposed changes it will be important to ensure measures are in place to streamline exemptions and authorisations regulatory arrangements and manage parallel frameworks.

There are a range of transitional issues that will need to be worked through carefully including, but not limited to:

- how to align selling arrangements between existing retailers and EN owners/operators under the existing market entry framework and the amended one
- how to extend any new and additional customer protections to embedded network customers covered under legacy arrangements.

Implementation issues and resourcing implications

Despite the transfer of some EN registration functions to AEMO, the AEMC's recommendations will have significant resource implications for the AER. Some relate to short-term tasks, but many will be ongoing. To support the changes the AER will need to review and revise most of its retail guidelines, the Network Guideline, and communicate and educate regulated parties and EN customers on their new obligations and rights. The changes will also result in the creation of a number of new functions and responsibilities for the AER (for example, compliance and reporting obligations) as well as the expansion of some existing functions (for example, authorising EN operators).

The AEMC's recommendations are also likely to have cost implications for EN operators and sellers. These costs may be passed on to customers. While we appreciate the AEMC is cognisant of the potential cost implications, we note any proposed changes to EN seller and operations frameworks should take these costs into account.

Gas embedded networks

We support the AEMC's intention to harmonise arrangements for gas embedded networks with the electricity regulatory framework and await further detailed proposals as to how this will be achieved.

Summary of key points

- **Measures to streamline the operation of parallel frameworks should be introduced**
- **The new and legacy frameworks should be aligned where possible**
- **Proposed changes will have significant resource implications for the AER and result in a number of new functions and responsibilities.**

Conclusion

We support the AEMC's proposed changes to the regulatory framework for ENs to increase competition in this sector and improve protections for EN customers. We agree significant changes to the design of the retail market and to the regulatory framework are essential to the effective operation of the market entry framework. Those changes are likely to add to the complexity of the EN market in particular and measures will need to be taken to mitigate this and address transitional and implementation issues.

Care needs to be taken in developing and implementing any changes to ensure the AER retains sufficient flexibility to make decisions and to respond to retail market developments. We welcome the development of a broader and more appropriate range of compliance tools to deal with the regulation of ENs and retail and network exemptions. We also support the proposed imposition of core customer protections and the establishment of retailer authorisation entry criteria, and point out the need for regulatory oversight of retrofitting activities. We note the particular implications of these changes in increased administrative costs, and the need to manage the complexity of administering the new framework alongside substantial legacy arrangements.

We look forward to continued collaboration with the AEMC and other stakeholders to identify and implement options for managing changes to the EN selling and operations frameworks. If you require further information about this submission or additional information or assistance please call Sarah Proudfoot on 03 9290 6965.

Yours sincerely



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Chair